SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: JUSTICE SHIRLEY WERNER KORNREICH PART 54
Justice

Underground Group, LLC,

- v -

Hali Power, Inc, et al,

INDEX NO. 650133/11
MOTION DATE 10/28/11
MOTION SEQ. NO. 004
MOTION CAL. NO.

The following papers, numbered 1 to 27-27-1 were read on this motion to/for dismiss

	PAPERS NUMBERED
Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...	27-27-1
Answering Affidavits — Exhibits	None - No Opp
Replying Affidavits	None

Cross-Motion: ☐ Yes ☒ No

Upon the foregoing papers, it is ordered that this motion

MOTION IS DECIDED IN ACCORDANCE WITH ACCOMPANYING MEMORANDUM DECISION AND ORDER.

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

Dated: 3/21/12

JUSTICE SHIRLEY WERNER KORNREICH
J.S.C.

Check one: ☐ FINAL DISPOSITION ☒ NON-FINAL DISPOSITION

Check if appropriate: ☐ DO NOT POST ☐ REFERENCE

☐ SUBMIT ORDER/ JUDG. ☐ SETTLE ORDER/ JUDG.

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 54

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UNDERGROUND GROUP, LLC,

Plaintiff,

Index No.: 650133/2011

-against-

HALI POWER, INC., SHENZHEN HALI POWER INDUSTRIAL CO., LTD., ZHUXIAO MIN a/k/a HARRY ZHU, EDWARD KANG, JING LI ZHANG a/k/a LILLIAN ZHANG AND MILI POWER LLC (as Nominal Defendant only),

DECISION and ORDER

Defendants.

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SHIRLEY WERNER KORNREICH, J.:

This action arises out of a failed business venture between plaintiff Underground Group, LLC (Underground) and its principal, non-party Marvin Jemal on the one hand, and defendants Hali Power Inc. (Hali), Shenzhen Hali Power Industrial Co., Ltd. (Shenzhen), Zhu Xiao Min (Zhu), Edward Kang (Kang) and Jing Li Zhang (Zhang) on the other.[1] The venture was to be conducted through the nominal defendant Mili Power LLC (Mili). In March of 2011, defendants Hali, Kang and Zhang (Movant Defendants) moved to dismiss pursuant to CPLR 3211(a)(1) and (7). By a decision and order dated July 5, 2011, the court denied the motion with leave to renew upon submission of hard copies of the motion papers in accordance with this part's rules. Having now submitted the proper papers, Movant Defendants renew their motion to dismiss. Plaintiff

[1] Shenzhen and Zhu, respectively, are a foreign corporation and a citizen of a foreign nation, though each allegedly does business in New York. Movant Defendants' counsel asserts that neither has been served in this action, and no evidence has been presented to the court that they were. Defs.' Mem. of Law, p. 1.

did not offer any opposition either to the original motion to dismiss or to the present motion to renew.

Background

The following facts are drawn from plaintiff's verified complaint and its accompanying exhibits.

On November 17, 2010, three documents were signed, the collective purpose of which was to establish a business venture to sell Chinese-made consumer electronic products in North America. Zhu on behalf of Hali and Jemal on behalf of Underground signed a Memorandum of Understanding (MOU). Zhu on behalf of Shenzhen and Jemal on behalf of Mili signed the Exclusive Agent Agreement (EAA). Zhu on behalf of Mili and Jemal on behalf of Underground signed the Exclusive Distributor Agreement (EDA).

Under the MOU, Hali and Underground were to form Mili with each contributing $10,000 in capital.[2] Hali was to transfer to Mili all of its sales and its rights as Shenzhen's exclusive agent for the distribution of its "Mili" brand electronic products in North America. Thereafter, it was to cease selling those products on its own. It could continue to register new products under the brand and to license the brand, but it was required to allocate all of the profits from such activities to Mili. These profits were then to be shared among the members according to their ownership interests.

Underground was to "transfer all of its sales" to Mili with certain enumerated exceptions.

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[2] In accordance with the MOU, Mili was later formed with Hali and Underground each having a 50% membership interest. Kang Aff., ¶ 18. However, defendant Kang attests that no operating agreement for Mili was ever entered into, and plaintiff does not allege otherwise. Kang Aff., ¶ 10.

Under the MOU, Mili's board was to be composed of five members–Zhu (as chairman), Jemal, Kang, Robert Grossman (who was previously associated with Underground) and an "outside board member." During the relevant period, this last position was filled by Stewart Mitchell. In addition, Jemal was to serve as CEO, Kang as COO, Grossman as executive vice president of sales and marketing, and Zhang as vice president of "Sales Middle and emergent Market."

Plaintiff alleges that shortly after entering into these agreements, defendants sought to wrest control of Mili from Jemal. On January 12, 2011, Zhu, purporting to act in his capacity as chairman of Mili's board of directors, sent Jemal a letter stating that, pursuant to a vote of the other members of the board, Jemal was being terminated as CEO and that Zhu was nominating Kang to fill his position. The next day, Kang acting as CEO advised Grossman in writing that he was being terminated as vice president of sales and marketing. He also notified Jemal, Grossman and another employee, Marc Zakaria, that as CEO, he was ordering that no further sales and shipments of Mili products be made from its offices.

Since that time, it does not appear that plaintiff or its principals have had the opportunity to profit from or participate in the business venture conducted through Mili. To the contrary, plaintiff alleges that defendants have, *inter alia*, refused to allow them to participate, failed to remit any profits from the venture, denied them access to Mili's website, wrongfully notified customers of the termination of Jemal and Grossman, wrongfully sold Mili products, and misappropriated Mili's customer list and information.

Plaintiffs seek the following: First Cause of Action: "an injunction enjoining the breach by the Defendants of the MOU, the EAA, and the EDA"; Second Cause of Action: a declaratory judgment as to the parties' rights under the contracts and money damages of $1,000,000.; Third

Cause of Action: "specific performance of the MOU, the EAA, and the EDA" and money damages of $1,000,000; Fourth Cause of Action: breach of the MOU, the EAA and the EDA, seeking regular and punitive damages; Fifth Cause of Action: tortious interference with contract by Zhu, Kang and Zhang; and Sixth Cause of Action: Zhu, Kang and Zhang "intentionally induced ShenZhen and Hali to breach the MOU, the EAA, and the EDA" and should pay $1,000,000 in damages and $5,000,000 in punitive damages.

Defendants' Opposition

Movants vigorously dispute plaintiff's account of what transpired. Broadly, they claim that plaintiff and its principals looted company funds and used its resources to carry out their own business activities while simultaneously failing to bring in any meaningful revenue. Kang Aff., ¶¶ 21-39. It was for these reasons–which they contend constituted a failure to perform all duties that may have been owed under the various documents–that they terminated Jemal and Grossman and ceased to carry on with the venture between the parties. *See id.*

Discussion

Dismissal pursuant to CPLR 3211(a)(7) (failure to state a cause of action) is required when, accepting the facts as alleged in the complaint as true and according the plaintiff the benefit of every possible inference, the facts alleged do not fit within a cognizable legal theory. *Leon v Martinez*, 84 NY2d 83, 87-88 (1994); *Skillgames, LLC. v Brody,* 1 AD3d 247, 250 (1st Dept 2003). Consequently, the inquiry on a motion to dismiss is narrow. *Tenzer, Greenblatt, Fallon & Kaplan v Ellenberg*, 199 AD2d 45 (1st Dept 1993) citing *Guggenheimer v Ginzburg*, 43 NY2d 268, 275 (1977); *Demicco Bros., Inc. v Con. Ed. Co.*, 8 AD3d 99 (1st Dept 2004). "However, factual allegations that do not state a viable cause of action, that consist of bare legal

conclusions, or that are inherently incredible or clearly contradicted by documentary evidence are not entitled to such consideration." *Skillgames*, *supra* quoting *Caniglia v Chicago Tribune-New York News Syndicate,* 204 AD2d 233, 233-234 (1st Dept 1994). Additionally, in assessing a motion under CPLR 3211, a court may freely consider affidavits submitted by the plaintiff to remedy any defects in the complaint. *Rovello v Orofino Realty Co., Inc.*, 40 NY2d 633, 635-636 (1976).

Defendant Zhang

The complaint contains no specific allegations of wrongful conduct by defendant Jinh Li Zhang. Instead, it makes conclusory statements, alleging that she "joined in, acquiesced to and countenanced" the "illegal, unjustifiable and wrongful actions" of the other individual defendants. Verified Compl., ¶ 54. While the court must view the facts in the light most favorable to the plaintiff, such broad, conclusory statements do not constitute factual contentions sufficient to state a cause of action. All claims against Ms. Zhang, therefore, are dismissed.

Defendant Kang

The first through fourth causes of action all allege that the "Defendants"–apparently all five excluding Mili itself–breached the MOU, EAA and EDA. "The elements of a cause of action for breach of contract are (1) formation of a contract between plaintiff and defendant; (2) performance by plaintiff; (3) defendant's failure to perform; and (4) resulting damage." *Clearmont Prop., LLC v Eisner*, 58 AD3d 1052, 1055 (3rd Dept 2009). Kang is not a party to any of these alleged agreements, and so all four claims must be dismissed as against him.

The fifth and sixth causes of action are for tortious interference with contractual relations against Kang, Zhang and Zhu. They are based, respectively, on "their termination of Grossman

and Jemal and by their instructions that Underground cease all sales and shipments of 'Mili' products," and on their having "intentionally induced ShenZhen and Hali to breach the MOU, the EAA, and the EDA." Verified Compl., ¶¶ 88, 93.

"A cause of action seeking to hold corporate officials personally responsible for the corporation's breach of contract is governed by an enhanced pleading standard." *Joan Hansen & Co. v Everlast World's Boxing Headquarters*, 296 AD2d 103 (1st Dept 2002). The complaint must allege, in "nonconclusory language," facts to show that "'the acts of the corporate officers were done with the motive for personal gain as distinguished from gain to their corporations.'" *Id.*, quoting *Potter v Minskoff*, 2 AD2d 513 (4th Dept 1956) *aff'd* 4 NY2d 695 (1958). The complaint does not state such nonconclusory facts, at least in regard to Kang. The conduct underlying the fifth cause of action appears to have been done in his capacity as an officer and director of Mili, and while the complaint makes the conclusory statement that they were "undertaken by [his] personal desire for monetary gain at the expense of Underground," there are no facts to suggest that he undertook them to personally gain at the expense of *Mili*. Indeed, there are no facts to suggest that he personally benefitted at all from Jemal's and Underground's exclusion from the venture. As for the sixth cause of action, plaintiff does not allege any facts to show how Kang caused either company to breach any of the agreements, and no facts show that he did so for his own personal benefit, as opposed to that of the companies. Thus, the fifth and sixth causes of action must be dismissed as to Kang.

Defendant Hali

As previously mentioned, the first through fourth causes of action all allege that the "Defendants"–including Hali–breached the MOU, EAA and EDA. Since Hali is not a party to

either the EAA or the EDA, to the extent that plaintiff has a viable claim for breach of contract against Hali, the claim can only be maintained in regard to the MOU. However, though clearly a signatory to the MOU, Hali denies that it is a binding agreement. It argues, instead, that the MOU is merely an unenforceable "agreement to agree." Defs.' Mem. of Law, p. 13, quoting *Joseph Martin, Jr. Delicatessen, Inc. v Schumacher*, 52 NY2d 105 (1981).

The scope and enforceability of "preliminary agreements" such as the MOU has been the subject of a great deal of litigation. Farnsworth, Farnsworth on Contracts, § 3.8a, at 230 (3rd ed.). The federal courts have traditionally divided preliminary agreements into two categories. "Type I" agreements, or "agreements with open terms," wherein "all essential terms have been agreed upon in the preliminary contract, no disputed issues are perceived to remain, and a further contract is envisioned primarily to satisfy formalities." *Shann v Dunk*, 84 F3d 73, 77 (1996). Such a contract is fully enforceable, at least in regard to the terms contained therein. *See id.*; *Teachers Ins. and Annuity Ass'n of America v Tribune Co.*, 670 FSupp 491 (SDNY 1987). Any missing, non-material terms may be implied by the court to effect the apparent intent of the parties, as would occur with any other contract for which such interpretation is necessary.

"Type II" agreements, on the other hand, are "agreements to agree". There, open terms exist and the parties "agree to bind themselves to negotiate in good faith to work out the terms remaining open." *Shann*, *supra*. Crucially, the parties do not bind themselves to the terms of the preliminary agreement. If after such good faith efforts no deal is reached, the preliminary agreement is unenforceable and neither party is bound by any terms contained within it. *See Teachers Ins.*, *supra*; Farnsworth, *supra* at 233.

Though it has accepted the reasoning underlying the Type I/Type II formulation, the Court

of Appeals has rejected the rigid categorization. *IDT Corp. v Tyco Group, S.A.R.L.*, 13 NY3d 209, 213 n 2 (2009). Instead, the Court in *IDT* views the operative question as "whether the agreement contemplated the negotiation of later agreements and if the consummation of those agreements was a precondition to a party's performance." *Amcan Holdings, Inc. v Canadian Imperial Bank of Commerce*, 70 AD3d 423, 427 (1st Dept 2010) *lv to appeal denied* 15 NY3d 704 (2010) quoting *IDT Corp.*, *supra*. If upon the evidence submitted this question is answered in the affirmative, the document constitutes, at most, an unenforceable agreement to agree. *Amcan Holdings*, *supra.*

Defendants contend that under this standard the MOU cannot, as a matter of law, be deemed to be an enforceable final agreement between the parties. Defs' Mem. of Law, pp. 12-14. This assertion is based on the premise that any agreement to form an LLC must contemplate the execution of an operating agreement, *see* NY LLC Law § 417(a)–which never occurred here–and that the MOU failed to set forth numerous terms material to any agreement to form an LLC. These include "the extent of the authority of officers" and the "criteria for making distributions." Defs.' Mem. of Law, p. 13.

The court disagrees. Neither of the complained-of shortcomings necessarily make the MOU so incomplete as to be unenforceable. First, most agreements to engage in complex transactions or business ventures contemplate the execution of additional instruments or agreements, *e.g.*, a contract for the sale of goods may contemplate the making of a negotiable instrument or the filing of a UCC-1 statement. The question is whether a document contemplates the execution of an additional written agreement covering the subject matter of the purported preliminary agreement. While the MOU may well contemplate the execution of an operating

agreement, it is not clear from its face that it contemplates a subsequent agreement in regard to the obligations plaintiff alleges defendant Hali assumed pursuant to it.

Second, though the NY LLC Law § 417(a) does require the execution of an operating agreement, it is not a precondition to the formation or initial operation of an LLC. Formation occurs upon filing of the article of incorporation, NY LLC Law § 203(d), while the operating agreement need not be filed for another 90 days. NY LLC Law § 417(c).

Third, the primary purpose of the LLC statute, like those covering corporations and other unincorporated business associations, is to provide all of the default rules necessary for the operation of the entity. As with partnership agreements and corporate by-laws, an LLC operating agreement serves to fill in any gaps left by the statute or to vary the default rules as desired by the equity holders and as permitted by law. Unsurprisingly then, the LLC statute provides default rules sufficient to cover most of the terms defendants note as absent from the MOU. To the extent that it does not, defendants fail to direct the court to any authority to show that those terms are so critical that their omission from the MOU makes it so incomplete as to be unenforceable.

In addition to the foregoing, it is significant that the parties appear to have performed at least some of the obligations set forth in the MOU. Partial performance is an important indicia of an intent to be bound by a writing. *R.G. Group, Inc. v Horn & Hardart Co.*, 751 F2d 69 (2nd Cir. 1984) ("Aside from unilateral contracts, partial performance is an unmistakable signal that one party believes there is a contract; and the party who accepts performance signals, by that act, that it also understands a contract to be in effect.") (applying New York law) citing *V'Soske v Barwick*, 404 F2d 495 (2nd Cir. 1968) (applying New York law) *cert denied* 394 US 921 (1969). Here, plaintiff alleges that it performed all of its obligations under the MOU, and while movants

deny this, they allege that Hali performed by providing its customer list to Mili and Underground and by taking steps to conduct the business contemplated by the MOU. Kang Aff., ¶¶ 16-39.

Finally, movants argue that since plaintiff failed to perform its obligations, if any, under the MOU, *id.*, and performance or readiness and willingness to perform is a necessary element of a claim for breach of contract, plaintiff has failed to state a cause of action. While this may be true, for the purposes of this motion the court must assume the truth of the allegations in plaintiff's verified complaint. Absent full discovery, dismissal on this ground is inappropriate.

The above notwithstanding, Hali is entitled to dismissal of the second cause of action which seeks "a judgment determining the rights, duties, obligations [sic] terms and conditions of Underground and Defendants pursuant to the MOU, the EAA and the EDA, including a judgment declaring that the MOU, the EAA and the EDA are enforceable against Defendants as written, and to pay to Underground money damages in an amount as of yet undetermined, but in any event not less than $1,000,000.00." Verified Compl., ¶ 73. "A cause of action for a declaratory judgment is unnecessary and inappropriate when the plaintiff has an adequate, alternative remedy in another form of action, such as breach of contract." *Apple Records v Capitol Records*, 137 AD2d 50, 54 (1st Dept 1988). Here, plaintiff has an "adequate, alternative remedy in another form of action"–a claim for breach of contract. Having asked for a money judgment in its request for a declaratory judgment, it would seem that plaintiff has acknowledged that it can be made whole through the legal remedy of damages alone.

Similarly, Hali is entitled to dismissal of that part of the third cause of action which seeks specific performance of the MOU. "In general, specific performance will not be ordered where money damages 'would be adequate to protect the expectation interest of the injured party.'"

Sokoloff v Harriman Estates Development Corp., 96 NY2d 409 (2001) quoting Restatement [Second] of Contracts § 359[1]. Specific performance is usually only appropriate "where 'the subject matter of the particular contract is unique and has no established market value.'" *Sokoloff, supra* quoting *Van Wagner Adv. Corp. v S & M Enters.*, 67 NY2d 186 (1986). Such contracts include those for the transfer of land or of goods that "are unique in kind, quality or personal association." *Sokoloff, supra* quoting Restatement [Second] of Contracts § 360. On the other hand, courts of equity are extremely reluctant to require specific performance of contracts that call for a series of acts over an extended period of time given the difficulty of judicial supervision of such conduct. *Grossman v Wegman's Food Markets, Inc.*, 43 AD2d 813 (4th Dept 1973); *Standard Fashion Co. v Siegel-Cooper Co.*, 157 NY 60 (1898) ("[c]ontracts which require the performance of varied and continuous acts ... will not, as a general rule, be enforced by courts of equity, because the execution of the decree would require such constant superintendence as to make judicial control a matter of extreme difficulty"). The MOU exemplifies the type of contract for which specific performance is inappropriate. It is not one that merely seeks the transfer of unique goods or a parcel of land. Instead, it contemplates all of the myriad actions required to carry on a joint business enterprise. Proper enforcement of such a contract would be nearly impossible for this court. Moreover, relief can be granted in the form of damages representing plaintiff's expected profits from the venture.

Last of all, Hali is entitled to dismissal of the request for punitive damages pursuant to the fourth cause of action for breach of contract. The purpose of punitive damages "is not to remedy private wrongs but to vindicate public rights." *Rocanova v Equitable Life Assur. Socy of U.S.*, 83 NY2d 603, 613 (1994). Contracts between private persons merely create private rights. *See*

Garrity v Lyle Stuart, Inc., 40 NY2d 354 (1976). A tort, on the other hand, is a violation of a duty imposed by law which exists "apart from and independent of promises made." *New York University v Continental Ins. Co.*, 87 NY2d 308 (1995) quoting Prosser and Keeton, Torts § 92, at 655 [5th ed.]. For this reason, in an action arising out of a breach of contract, a plaintiff must allege that: (1) the defendant engaged in conduct rising to the level of an independent tort; (2) the conduct "evinced a high degree of moral turpitude and demonstrated such wanton dishonesty as to imply a criminal indifference to civil obligations"; (3) the conduct was directed at the plaintiff; and (4) the conduct was directed towards the public generally. *New York University v Continental Ins. Co.*, *supra*, citing *Walker v Sheldon*, 10 NY2d 401 (1961); *Rocanova*, *supra*. When these elements are present, the public then has an interest which may be vindicated through the imposition of punitive or exemplary damages, which both compensate for harm caused to the public and deter such action against the public in the future. *New York University*, *supra*.

Plaintiff's allegations fail to meet the standard set forth in *New York University*. Plaintiff has not alleged that Hali engaged in any tortious conduct separate from the conduct underlying the claim for breach of contract. Nor has it set forth any facts to show that Hali acted with "such wanton dishonesty as to imply a criminal indifference to civil obligations" or that any tortious conduct it might have engaged in was directed towards the public generally. Moreover, "where a party is merely seeking to enforce its bargain, a tort claim will not lie." *New York University*, *supra* at 316. Here, plaintiff is not seeking rescission on the ground of fraudulent inducement or damages pursuant to tortious conduct independent of Hali's alleged contractual duties. Instead, it is seeking enforcement of its alleged bargain–indeed, it is seeking specific performance. Punitive damages are therefore unavailable. Accordingly, it is hereby

ORDERED that the motion of defendants Hali Power, Inc., Edward Kang and Jing Li Zhang, a/k/a, Lillian Zhang to renew, is granted, on default; and it is further

ORDERED that, upon renewal, this court vacates its prior order dated July 5, 2011; and it is further

ORDERED that, to the extent that it seeks dismissal of the Causes of Action for injunctive and declaratory relief and specific performance, it is granted and the First, Second and Third Causes of Action are dismissed; and it is further

ORDERED that the motion to dismiss the action as against defendants Edward Kang and Jing Li Zhang, is granted, the complaint is dismissed in its entirety as against defendants Edward Kang and Jing Li Zhang, a/k/a, Lillian Zhang, with costs and disbursements to said defendants as taxed by the Clerk of the Court, and the Clerk is directed to enter judgment accordingly in favor of said defendants, and the Clerk shall enter judgment accordingly; and it is further

ORDERED that the remainder of the action is severed and continued as to the remaining defendants, Shenzhen Hali Power Industrial Co., Ltd., Zhuxioa Min, a/k/a, Harry Zhu, and Mili Power LLC, as nominal defendant; and it is further

ORDERED that the caption be amended to reflect the dismissal of said defendants and that all future papers filed with the court bear the amended caption; and it is further

ORDERED that insofar as plaintiff alleges that defendant Hali Power, Inc. breached the EDA and the EAA and seeks punitive damages in the fourth causes of action, those allegations are dismissed, but insofar as they allege breach of the MOU, the fourth cause of action against Hali remains; and it is further

ORDERED that within 20 days of the date of this order, defendant Hali Power, Inc. is directed to serve upon plaintiff an answer to the complaint along with a copy of this order with notice of entry; and it is further

ORDERED that the parties shall appear for a status conference on April 26, 2012, at 9:30 AM in Room 228, 60 Centre Street, New York, New York; and it is further

ORDERED that if plaintiff does not appear by counsel at this status conference or make a timely request for an adjournment to a more convenient date, this action will be dismissed pursuant to Section 202.27(b) of the Uniform Civil Rules for the Supreme Court; and it is further

ORDERED that counsel for the moving parties shall serve a copy of this order with notice of entry upon the County Clerk and the Clerk of the Trial Support Office, who are directed to mark the court's record to reflect the change in the caption herein; and it is further

ORDERED that the Clerk shall enter judgment accordingly.

Dated: March 21, 2012

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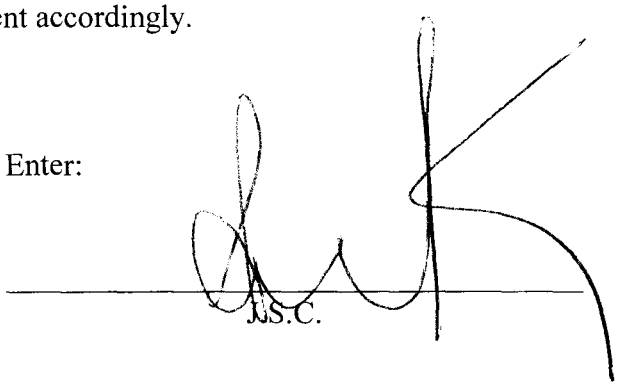

J.S.C.